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Supreme Court of the United States

OCTOBER TERM, 1934.

~~No. 475.~~

FOX FILM CORPORATION,

Petitioner,

vs.

A. B. MULLER,

Respondent.

RESPONDENT'S BRIEF.

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Supreme Court of the United States

OCTOBER TERM, 1934.

No. 478.

FOX FILM CORPORATION,

Petitioner,

vs.

A. B. MULLER,

Respondent.

ON WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF MINNESOTA.

RESPONDENT'S BRIEF.

STATEMENT OF THE CASE.

I. INTRODUCTION.

The petitioner, Fox Film Corporation, invoked the jurisdiction of the District Court for the Fourth Judicial District of Minnesota against the respondent, A. B. Muller, to recover the stipulated rentals for certain motion pictures licensed by the petitioner for exhibition by the respondent in his motion picture theatre in Maple Lake, Minnesota, which pictures were not accepted or exhibited by the respondent (R. 1-9).

No issue was raised as to the execution of the contracts or

the failure of the respondent to accept and exhibit the pictures (Stipulation R. 22; Complt. R. 2-7). The defense was based on the illegality and lack of mutuality of the contracts sued upon.

The printed portions of the contracts sued upon were substantially similar to the Standard Exhibition Contract condemned by this Court under the Sherman Anti-Trust Act in *Paramount vs. United States,* 282 U. S. 30 (R. 22).

II. Defenses Set Up in the Answer.

Respondent's amended answer attacked the contracts on three grounds:

1. That they were a part of a conspiracy among the distributors of motion pictures (including the petitioner) in violation of the Sherman Act (R. 10-12, 18).

2. That the provisions of said contracts were in and of themselves in restraint of trade (R. 12-17, 18).

3. That the contracts were unilateral (R. 18-20).

Respondent denies that the only defense urged was that the contracts were illegal and unenforceable because they contained the compulsory arbitration clause condemned in the *Paramount Case,* as claimed by the petitioner (Br. 3).

On the contrary, respondent's amended answer attacks the contracts in their entirety, as well as the manner in which they were imposed upon him. No right or privilege under the decision or decree in the *Paramount Case* was specially set up or claimed by the respondent. Neither did respondent offer the decree in evidence as he was authorized to do by Section 5 of the Clayton Act (Act of October 15, 1914, 38 Stat. 730; U. S. Code Tit. 15, Ch. I, Sec. 16).

The issues in the present case are much broader than those raised by the Government in the *Paramount Case.*

III. Decisions of the State Courts.

Notwithstanding the breadth of the amended answer, both the State District Court (R. 57-63, 73) and the State Supreme Court (R. 77-83) chose the easy way and held the contracts illegal on the authority of *Paramount vs. United States* and the several State and Federal decisions to the effect that the ruling of the Court in the *Paramount Case* invalidated not merely the compulsory arbitration clause of the Standard Exhibition Contract but the entire contract, for the reason that said clause is not severable from the remainder of the contract.

The decision of the Supreme Court of Minnesota is reported in 255 N. W. Rep. 845; the decision of the District Court is not reported.

IV. Issue Raised by the Petitioner.

Petitioner takes the position, in effect, that the decree of the United States District Court for the Southern District of New York in *United States vs. Paramount,* to which neither the respondent nor any representative body of motion picture exhibitors was a party, is *res judicata* in the present case, and that the Supreme Court of Minnesota misinterpreted said decree and hence failed to give full faith and credit to the same (Pet. for Certiorari, 1-2, 7, 15; Br. 6, 23).

ARGUMENT.

POINT I.

THE DECREE IN THE PARAMOUNT CASE IS NOT A LIMITATION ON THE POWER OF THE COURTS OF MINNESOTA TO RELIEVE THE RESPONDENT AGAINST THE MONOPOLISTIC AND ONE-SIDED STANDARD EXHIBITION CONTRACT.

1. *The decree is not res judicata.* This follows for the simple reason that there is neither identity of parties or of issues in the two proceedings. *Paramount vs. United States* was a suit in equity brought by the Government to enjoin the carrying out of a conspiracy in restraint of trade in violation of the Sherman Anti-Trust Act (Act of July 2, 1890, 26 Stat. 209; U. S. Code Tit. 15, Ch. I, Secs. 1, 4). It is admitted that the petitioner, Fox Film Corporation, "was one of the defendants named in said action and said opinion of the United States District and Supreme Court" (Stip. R. 22). The respondent, Muller, was not, however, a party to the proceeding either directly or by representation.

Moreover, the petition filed by the Government, while attacking broadly the conspiracy among the several distributor-defendants, was not as far-reaching in its attack on the Standard Exhibition contract as the answer in the present case. Unlike this answer said petition did not attack provisions of the Standard Exhibition contract (other than the compulsory arbitration clause) as illegal in and of themselves, and made no point of the unilateral nature of the contract.

2. *Paragraph 3 of the decree does not validate the contract.* Respondent challenges the claim made by petitioner that the proviso in Paragraph 3 of the decree validates and makes enforceable provisions of the Standard Exhibition

contract other than the compulsory arbitration clause. Said proviso reads:

> "Nothing contained in this decree shall be construed as prohibiting any defendant or any member of any defendant Film Board of Trade from performing and/or continuing to perform, or enforcing or continuing to enforce, by any lawful means any contractual obligation the performance or enforcement of which is consistent with the provisions of this decree" (Appendix B to Petitioner's Brief, p. 35).

The obvious meaning of this proviso is that it shall not be considered a contempt of court for any of the defendants to vindicate or seek to vindicate whatever legal rights they may possess. Clearly the District Court in the *Paramount Case* could not determine the rights of persons not parties to that suit or preclude other courts from adjudicating such rights.

Sub-paragraph 8 of Paragraph II, also cited by the petitioner (Br. 8), is similarly explained. This provision enjoins the defendants from suspending or refusing promptly to resume service to any exhibitor because of any failure or refusal to comply with the compulsory arbitration clause. This is but a corollary to the provisions specifically enjoining the enforcement of the arbitration clause. It is ridiculous to suppose that this injunctive provision conferred any rights on the defendants or denied any rights to persons not parties to the suit.

The claim of the petitioner, if sustained, would lead to monstrous results. The rights of all citizens and the powers of all other courts in important Anti-Trust cases would be subject to the determination of United States District Courts in cases brought by the Federal Government wherein

the decrees are usually settled upon such terms and conditions as the lawyers representing the Government for the time being may see fit to demand or yield.

Point II

The Courts of Minnesota Rightfully Refused to Aid the Petitioner in Its Efforts to Enforce the Illegal Standard Exhibition Contract Against the Respondent.

1. *The entire contract is unenforceable under the decision in the Paramount Case.* We submit that the petitioner, not the courts below, has misinterpreted the scope and effect of the opinions and decree in the *Paramount Case*. The case not only is not a limitation on the power of the State courts to declare the entire Standard Exhibition Contract invalid, but is an authority for so ruling.

The contracts sued on are not collateral to the illegal conspiracy among the motion picture distributors—including the petitioner—condemned by this Court. These contracts are an essential part—the visible manifestations—of that conspiracy. The conspiracy consisted in an unlawful agreement to impose upon the theatre owners this uniform contract.

This Court said:

> "The record discloses that ten competitors in interstate commerce, controlling sixty per cent of the entire film business, have agreed to restrict their liberty of action by refusing to contract for display of pictures except upon a Standard Form which provides for compulsory joint action by them in respect of dealings with one who fails to observe such a contract with any Distributor, all with the manifest purpose to coerce the

Exhibitor and limit the freedom of trade" (282 U. S. 30, 41).

District Judge Thacher in rendering the decree thus affirmed by this Court, said:

> • • • "One can hardly imagine a more direct restraint upon trade than an agreement between competitors in an open market not to trade except upon terms which they have fixed in advance" (34 Fed. (2d) 984, 988).

The decree, Paragraph I, provides:

> Ordered, Adjudged and Decrees as follows:
>
> "That the agreement of the defendants to adopt and to use exclusively in contracting with exhibitors of motion pictures throughout the United States the 'Standard Exhibition Contract,' dated May 1, 1928, which is attached to the petition herein as Exhibit 'C' thereto, the adoption by the defendants of the 'Rules of Arbitration,' dated May 1, 1928, which is attached to the petition herein as Exhibit 'G' thereto, and all the activities and agreements of said defendants by means of which they have collectively coerced adoption of and compliance with said 'Standard Exhibition Contract' and said 'Rules of Arbitration,' constitutes a conspiracy in restraint of interstate trade and commerce in violation of the Act of Congress of July 2, 1890, entitled 'An Act to protect trade and commerce against unlawful restraints and monopolies,' known as the Sherman Anti-Trust Act."

Paragraph II provides, in part, as follows:

> "That the defendants, their officers, agents, servants and employees, and all persons acting under, through

or on behalf of them, or any of them, hereby are perpetually enjoined, restrained and prohibited, individually and collectively

1. From further engaging in or carrying out said conspiracy or any other conspiracy similar to or having the same purpose and/or effect as said conspiracy.

2. From doing any act or thing whatsoever for the purpose or with the effect of carrying on hereafter the purposes of said conspiracy or any of them."

The remaining injunctive provisions are aimed particularly at Paragraph 18 (the compulsory arbitration clause) of the Standard Exhibition Contract and Rule IV of Arbitration Rules. But the fact remains that the conspiracy to agree upon and enforce the Standard Contract and the Arbitration Rules was the gist of the offending against the Sherman Act.

The refusal of the Minnesota courts to enforce the Standard Contract—the reason for and product of the illegal conspiracy—was consistent with and not contrary to the opinions and decree in the *Paramount Case.*

2. *The contracts sued on are not collateral to but are the embodiment of the illegal conspiracy.* The courts of Minnesota could not enforce the Standard Exhibition Contract without sanctifying the illegal conspiracy which gave it birth and aiding one of the conspirators in oppressing one of its victims.

While courts will not refuse to enforce contracts which are purely collateral to an illegal conspiracy, they will not give effect to contracts which are essential parts of such a conspiracy. The case of *Continental Wall Paper Company vs. Voight,* 212 U. S. 227, relied on by the lower courts (R.

61, 83) makes clear this distinction and is a perfect authority in this case.

In the course of this notable opinion Mr. Justice Harlan said (pp. 260-261):

"The present case is plainly distinguishable from the *Connolly Case*. In that case the defendant, who sought to avoid payment for the goods purchased by him under contract had no connection with the general business or operations of the alleged illegal corporation that sold the goods. He had nothing whatever to do with the formation of that corporation and could not participate in the profits of its business. *His* contract was to take certain goods at an agreed price, nothing more, and was not in itself illegal, *nor part of nor in execution of any general plan or scheme that the law condemned.* The contract of purchase was wholly collateral to and independent of the agreement under which the combination had been previously formed by others in Ohio. It was the case simply of a corporation that deals with an entire stranger to its management and operations and sold goods that it owned to one who wished to buy them. In short, the defense in the *Connolly Case* was that the plaintiff corporation, although owning the pipe in question and having authority to sell and pass title to the property, was precluded by reason *alone* of its illegal character from having a judgment against the purchaser. We held that the defense could not be sustained either upon the principles of the common law or under the Anti-Trust Act of Congress.

The case now before us is an entirely different one. The Continental Wall Paper Company seeks, in legal effect, the aid of the Court to enforce a contract for the sale and purchase of goods, which, *it is admitted by the*

demurrer was in fact and was intended by the parties to be based upon agreements that were and are essential parts of an illegal scheme." (Italics by Mr. Justice Harlan.)

The rule has been more succinctly stated by Mr. Justice Van Devanter in *A. B. Small & Company vs. Lamborn & Company*, 267 U. S. 248, 252, as follows:

> "As has been pointed out in prior cases, there is nothing in the Anti-Trust Act which invalidates such a collateral contract or relieves the buyer from his obligation under it * * * It is only where the invalidity is inherent in the contract that the Act may be interposed as a defense."

This same distinction was made by Mr. Chief Justice White in *D. R. Wilder Mfg. Co. vs. Corn Products Refining Co.*, 236 U. S. 165, in the excerpts from his opinion quoted in petitioner's brief, pages 16 to 18.

Thus do all of the authorities cited and relied on by the petitioner (Br. 15) distinguish themselves from the case at bar. Another point of distinction between this case and *Connolly vs. Union Sewer Pipe*, 184 U. S. 540, and the *Wilder Case, supra*, is that the motion pictures here in question were not accepted or exhibited by the respondent, hence there is no possible question of a recovery on *quantum meruit*.

Another point of similarity between the present case and *Continental Wall Paper Co. vs. Voight* is that counsel for the respondent at the trial, evidently impressed by the connection between the seller and the buyer in the latter case, proved and the petitioner now concedes (Br. 4) that the president of the Motion Picture Theatres of the Northwest, representing that Association, of which the respondent is a

member, was one of the exhibitor leaders mentioned in the opinion of District Judge Thacher in the *Paramount Case* as having participated in the formulation of the Standard Exhibition Contract.

Point III.

Paragraph 18 of the Standard Exhibition Contract Being Admittedly Illegal, the Remainder Is Unenforceable For the Reason That Said Paragraph Goes to the Heart of the Contract and Is Not Severable.

1. *The illegality of Paragraph 18 is established and conceded.* While petitioner has labored to narrow the scope and effect of the decision in the *Paramount Case* in other respects, it does not deny that said decision rendered Paragraph 18 (the compulsory arbitration clause) illegal (Stip. R. 22-23). Petitioner has taken pains to point out that "in this litigation (it) made no claim under Paragraph Eighteenth" (Br. 4).

Petitioner's position is, in effect, "Strike out Paragraph 18 and enforce the rest of the contracts."

This overlooks the fact that Paragraph 18, whatever its other infirmities, afforded the respondent a valuable means —and the only readily available means—for protecting his rights under the contracts here involved. The rule may be, in certain classes of cases, as contended by petitioner (Br. 11) "that the bad parts do not affect the good"; but this does not apply where removal of the bad also removes an important part of the consideration for making the contract, or where the good is inseparably connected with and dependent upon the bad.

2. *Paragraph 18 afforded respondent the only readily available means for protecting his rights under the con-*

tracts.[1] The Standard Exhibition Contract was aptly described by Mr. Justice McReynolds as "an elaborate document." The complications of the business are such as to preclude simplicity. A great many contingencies, unknown to other industries must be provided for. Each such provision can and does give rise to controversies between the distributors and exhibitors. But the distribution and exhibition of pictures can not halt pending the settlement of such controversies. If the distributor refuses to furnish the exhibitor with a picture that he feels he is entitled to, he can not litigate the matter for weeks or months. A picture can become stale and lose its box office value in a very short period of time. The only remedy that can be of value to the exhibitor must be readily available and speedily consummated. The arbitration clause was a valuable part of the contract so far as the exhibitor is concerned. The rules under which this arbitration was conducted and awards in favor of distributors enforced were unfair. Except for this, Paragraph 18 provided an ideal method of settling disputes and was immensely valuable to the exhibitors.

The importance of the arbitration clause to the exhibitors will be appreciated when it is considered that the damage to the distributor for failure on the part of the exhibitor to play a picture in accordance with his contract is the rental fixed in the contract for that picture. Liquidated damages are not provided for the exhibitor in case the distributor fails or refuses to deliver a picture contracted for. The exhibitor is left practically remediless since the damage suffered is the wholly speculative difference between what the

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[1]Petitioner has kindly printed the contract in readable type as Appendix A to its brief, and reference will be made to this rather than to the copy in the record which is printed in such fine type as to be almost illegible.

picture in question might have drawn and what some makeshift substitute actually drew. Under Paragraph 18 the exhibitor in such circumstances could appeal to the Arbitration Board and have his right to the picture established while the same is fresh and a matter of current interest in his community.

Because of its importance to the exhibitor Paragraph 18 undoubtedly constituted a major inducement for entering into the contracts on which petitioner stakes its case.

3. *The relation of Paragraph 18 to other paragraphs of the Standard Exhibition Contract demonstrates non-severability.* Every other provision of the contract is directly related to Paragraph 18. With Paragraph 18 removed from the contract the rights of the exhibitor under the remaining provisions are largely dependent upon the indulgence of the distributor. The following is an enumeration of problems arising under the other paragraphs which in the absence of some method of arbitration can not be settled within permissible limits of time and the means of the average small exhibitor:

Paragraph First: Inclusion of unwarranted provisions in the Standard Form by means of riders or otherwise.

Paragraph Second: (a) Identification of the pictures included in the contract.

(b) Determination of rights with respect to pictures not generally released during the term of the contract.

Paragraph Third: Questions as to alleged unauthorized exhibitions.

Paragraph Fourth: Questions relating to timeliness of payments.

. . . . . .

Paragraph Sixth: Vitally important questions as to

"run" (*i. e.*, first, second, or third in a competitive situation) and "protection" (*i. e.*, the period of time which must elapse before a subsequent run theatre can follow a prior run).

Paragraph Seventh: Disputes as to the timeliness of the delivery and return of prints, including damage to prints while in the exhibitor's possession. This paragraph expressly provides that damages caused by delay in the return of prints "shall be determined by Arbitration as provided for in Article Eighteenth hereof."

Paragraph Eighth: The multitudinous controversies which can and do arise out of the complicated provisions for the selection or designation of play dates.

Paragraph Ninth: Replacement of film damaged or lost while in the exhibitor's possession.

Paragraph Tenth: Disputes growing out of attempts by the distributor to substitute other pictures for the ones actually sold.

Paragraph Eleventh: Disputes growing out of the assignment of contracts upon the sale of a theatre.

Paragraph Twelfth: Disputes arising out of attempts by the distributor to control the exhibitor's advertising and his use of advertising accessories.

Paragraph Thirteenth: Disputes arising out of the inclusion of paid advertising in the pictures themselves.

Paragraph Fourteenth: Disputes arising out of attempts by the distributor to cast upon the exhibitor the burden of all taxes imposed or based upon the "delivery" as well as the "exhibition" of pictures.

Paragraph Fifteenth: Disputes growing out of attempts by the distributor to regulate the admission prices of the theatre.

Paragraph Sixteenth: Disputes growing out of delays in

exhibition or delivery due to causes beyond the control of the parties.

* * * * * * * * *

Paragraph Twentieth: Disputes arising out of the exercise by the exhibitor of his right to exclude certain pictures from the block upon payment of one-half of the rental, including disputes as to the computation of such rentals on percentage bookings.

Paragraph Twenty-first: Disputes as to pictures deemed offensive to the public because of racial or religious subject-matter, this provision also being expressly coupled with the arbitration clause.

Paragraph Twenty-second: Disputes as to whether an application for a contract has been accepted within the periods specified.

What has been said with reference to the foregoing provisions of the contract applies equally to the approved additional clauses (Pet. Br., App. "A," pp. 21-26).

4. *The better reasoned decisions are to the effect that Paragraph 18 is not severable.* The cases so holding are as follows:

Majestic Theatre, Inc., vs. United Artists, 43 Fed. (2) 991;
Vitagraph vs. Theatre Realty Co., 50 Fed. (2) 907;
Fox Film vs. C & M Amusement Co., 58 Fed. (2) 337;
Universal Film Exchange vs. West (Miss.), 141 So. 293;
Fox Film vs. Tri-State Theatres (Idaho), 6 Pac. (2) 135;
United Artists Corp. vs. Piller (N. D.), 244 N. W. 20;
United Artists Corp. vs. Odeon Building, Inc. (Wisc.), 248 N. W. 784.

In *Fox Film vs. C & M Amusement Co., supra*, it was held

that the illegal elements are inseparable from the contract, the court saying on page 339, as follows:

> "The fraudulent and illegal elements permeating these contracts must, it seems to the court, taint and void the entire contract so far as it may affect or bind one who through the medium of coercion has become a party to it.
>
> The defendant in this case does not find itself in the collateral position, as was the case in the line of decisions wherein the principle was laid down that one purchasing and receiving the goods and afterwards learning that the seller was a party to an illegal combination and refused to pay for them could avoid the contract. *Connolly vs. Union Sewer Pipe Co.*, 184 U. S. 540, 22 S. Ct. 431, 46 L. Ed. 679; *Continental Wall Paper Co. vs. Louis Voight & Sons Co.*, 212 U. S. 227, 29 S. Ct. 280, 53 L. Ed. 486; *Small Co. vs. Lamborn & Co.*, 267 U. S. 248.
>
> After having the value and benefit of the purchased goods, the courts granted protection to the seller, notwithstanding his illegal situation, on the basis that otherwise the buyer would receive something for nothing."

In *Universal Film Exchange vs. West, supra,* in holding that the entire contract is illegal and void, the court said:

> "In the determination of the question whether the illegal portion of a contract may be severed from the remainder, it is not permissible to simply strike out and wholly disregard the illegal portion as if it had never been a part of the agreement. *McMullen vs. Hoffman,* 174 U. S. 639, 19 S. Ct. 839, 43 L. Ed. 1117. On the contrary, the illegal as well as the legal portions must be

taken into view and thereupon the question, to state it tersely, is whether there is a vital connection between the illegal portion and the other portions. Another statement of the rule is that even though it may be possible to sever the illegal from the legal portion of the contract, yet, if there are no means by which to ascertain whether the promise was induced by the legal or illegal portion, the entire contract will be held illegal if one of the material elements thereof is unlawful. 3 *Elliott Contracts,* pp. 350, 351. Here we have a case before us which falls not only within the rule as last stated, but which comes within the rule of vital connection first mentioned; for it is expressly stipulated in the contract, and here we call particular attention to the third paragraph of the eighteenth or arbitration section of the contract copies above, that, unless the said unlawful provision shall be complied with by the exhibitor, the distributor shall have the right to terminate the contract. In other words the contract expressly provides that, unless the exhibitor shall be bound by and shall observe the illegal portion of the agreement, the distributor shall not be bound by any of the said contract, but may wholly terminate it. Therefore the illegal portion inseparably and vitally connects itself with all the other parts, and, in consequence, the illegal portion infects the entire contract with illegality."

In *Fox Film Corp. vs. Tri-State Theatres, supra,* it was held that the execution of this contract within prohibition of the Sherman Anti-Trust Act in whole or in part, is wholly unlawful.

The court in its opinion, stated:

"The contention on which the appellant bases its case

is the claim that 'The arbitration clause is separable from the other parts of the contract and its illegality neither affects the remainder of the contract nor relieves the defendant from its obligation to perform the legal covenants to receive and pay for motion pictures.'

In conclusion, as we understand the law, a contract which is within the prohibition of the Sherman Anti-Trust Act in whole or in part is not only illegal but its execution is unlawful. The act of executing it is a misdemeanor under the laws of the United States. The complaint here virtually alleges that a part of the contract in suit is illegal as prohibited by the Sherman Anti-Trust Act. If so, its execution was unlawful."

On petition for rehearing, the court said:

"In this case the petition does not come to the real point. In the case of *United States vs. Paramount-Famous Lasky Corporation, supra,* the action was to restrain further use of the contract. The court held that the contract, including clause 19 (sic) as written, was in violation of the Sherman Anti-Trust Act, and further held that by striking out that clause the contract would then not offend. In this case, however, the action is on contract. The complaint alleges that the clause was not stricken out, that it was part of the contract as executed, but further alleges that the contract with that clause in it is illegal as in restraint of trade and violative of the Sherman Anti-Trust Act. We have simply held that, if this is so, the contract is not an illegal contract, but was unlawfully executed and therefore unenforceable. That is the main point in the case and petition for rehearing avoids that point all the way through."

In *United Artists vs. Piller* (N. D.), *supra*, on the question whether or not the illegal portion of the contract was severable from the rest of the contract, the court said:

> "On the contrary, the illegal as well as the legal portions must be taken into view, and thereupon the question to state it tersely, is whether there is a vital connection between the illegal portion and the other portions. Another statement of the rule is that even though it might be possible to sever the illegal from the legal portion of the contract, yet, if there are no means by which to ascertain whether the promise was induced by the legal or illegal portion, the entire contract will be held illegal if one of the material elements thereof is unlawful. 3 *Elliott Contracts*, pp. 350, 351. Here we have a case before us which falls not only within the rule as last stated, but which comes within the rule of vital connection first mentioned; for it is expressly stipulated in the contract, and here we call particular attention to the third paragraph of the eighteenth or arbitration section of the contract copies above, that, unless the said unlawful provision shall be complied with by the exhibitor, the distributor shall have the right to terminate the contract. In other words, the contract expressly provides that, unless the exhibitor shall be bound by and shall observe the illegal portion of the agreement, the distributor shall not be bound by any of the said contract, but may wholly terminate it. Therefore the illegal portion inseparably and vitally connects itself with all the other parts, and, in consequence, the illegal portion infects the entire contract with illegality."

In *United Artists Corporation vs. Odeon Building, Inc.*

(Wisc.), *supra*, after quoting with approval the above quotation from *United Artists vs. Piller*, 244 N. W., the Wisconsin Supreme Court said:

> "It appears to us that the weight of authority, as well as sound reason, supports the conclusions, first, that the arbitration clause is unquestionably illegal; and, second, that its inclusion so influenced the making of the contract as to render its separation from the legal portion of the contract improper. The fight made to sustain the arbitration clause in the litigation which culminated in *Paramount-Famous Lasky Corporation vs. United States, supra*, would seem to indicate its general importance to the combination plan. The arbitration clause provides, that, in the event that the exhibitor shall fail or refuse to submit to arbitration, the distributor may at its option, demand security for its protection, and upon failure to comply with such demand, may suspend service or terminate the contract. It seems clear, from these provisions, that the arbitration plan embodied in the contract is so closely connected and tied into the remainder of the contract that it must be said that the illegality permeates the whole contract."

This question is also discussed in a well written article on this subject appearing in the Yale Law Journal for the month of January, 1933, beginning at page 431; the writer of such article, after discussing all of the cases decided on this point pro and con, reaches the conclusion that the majority of the decisions on the subject are to the effect that the contract is entirely illegal and void, by reason of being in violation of the Sherman Anti-Trust Act.

5. *Contrary decisions considered.* In the case of *Columbia Pictures vs. Bi-Metallic Investment Co.*, 42 Fed. (2d)

873, the decision of the court is upon a demurrer of the defendant (exhibitor) to the plaintiff's complaint. The contract was not before the court. The arbitration clause was not involved, since it was not referred to in the complaint, and the court therein stated that unless the arbitration clause is brought to the attention of the court by pleadings not yet filed, it was not necessary to a decision on the demurrer. In other words, the court in that case did not pass upon the legality of the entire contract.

In *Paramount-Famous Lasky Corporation vs. National Theatre Corp.*, 49 Fed. (2) 64, plaintiff filed a complaint against the defendant, alleging breach of the contract to exhibit certain pictures, which it was alleged plaintiff furnished, and for which the defendant agreed to pay. The defendant demurred to the complaint, and claimed the plaintiff had failed to comply with a condition precedent, to-wit, to arbitrate the claim, as provided in Section 18 of the contract. On appeal, the Circuit Court of Appeals held that arbitration was not a condition precedent, since it had been held to be illegal, and accordingly overruled defendant's demurrer.

The case of *Metro-Goldwyn-Mayer vs. Bijou Theatre*, 50 Fed. (2d) 908, is not material to the issues herein involved, since that case was an action to restrain the defendant from infringing plaintiff's copyright.

In the case of *Fox Film Corp. vs. Buchanan* (La.), 136 So. 197, the Supreme Court of Louisiana erroneously proceeded upon the theory that the action was one to recover for goods sold and delivered, overlooking entirely that the contract sued upon was executory, and that the action was prosecuted for the alleged refusal of the defendant to accept and use the photoplays.

In *Fox Film Corp. vs. Ogden Theatre Co.* (Utah), 17 Pac.

(2) 294, the court erroneously assumed that the Thacher decree provided that the arbitration clause alone was illegal.

In none of the cases above referred to, was the entire decree of Judge Thacher before the court.

However, the entire decree was before the trial court in this case, and in his memorandum, Judge Guilford concludes as follows (R. 62-63):

> "It is claimed, however, by plaintiff that language contained in the decree of the Federal District Court of New York contains a severing clause which indicates the intention of the court that the injunction should not be construed as preventing the distributor from enforcing the contract, in so far as such enforcement is consistent with the decree. This severing clause, so-called, would be clearer if after the words 'contractual obligation' there appeared the words 'theretofore made.' But if such were the intention of the Federal District Court it does not appear from the decision of the Supreme Court of the United States affirming that decision that the latter court intended to depart from its well settled rules as to the effect of a violation of the anti-trust law on contracts, as declared in the *Continental Wall Paper* and other cases. Before we can conclude that the effect of the decision was such as plaintiff claims it ought to be very clear. In the Idaho case, the court, after reviewing the opinions of both the trial and the Supreme Court, concludes that the Supreme Court, at least, intended to hold void the entire contract.
>
> I have, therefore, come to the same conclusion as is expressed in the concluding paragraphs of the Idaho and North Dakota decisions, to-wit:

A contract which is within the prohibition of the Sherman Anti-Trust Law in whole or in part is not only illegal but its execution is unlawful.

Attention is called to a note in the Yale Law Journal, January, 1933, Volume 42, No. 3, in which the cases are reviewed. The author gives as one of the reasons for concluding that the contract is not severable the reason that the arbitration clause is of the essence of the contract, in that it provides the machinery for regulation of relations between the distributor and exhibitor; that since the avowed purpose of the entire contract and arbitration agreement is to establish the sphere of self-government for the industry, it seems beyond doubt that the arbitration clause is vital and of the essence of the contract.

I have therefore concluded plaintiff is not entitled to recover in an action on the contract. Possibly where films have been delivered an action may lie in *quantum meruit.*"

6. *Necessity for fair arbitration recognized by N. R. A.* Although the record was closed before this development, it is believed that counsel for the petitioner will indulge the statement that following affirmance of Judge Thacher's decree by this Court the distributors adopted and made available to the exhibitors a form known as "Optional Standard License Agreement" containing an eminently fair arbitration clause to be executed separately at the option of the respective parties. The Code of Fair Competition for the Motion Picture Industry, approved by the President November 27, 1933, provides, in Division F, Part 1:

"The so-called Optional Standard License Agreement (1933) negotiated by Exhibitors and now being used by

a large number of Distributors shall be the form of license contract to be used by Distributors for licensing the exhibition of motion pictures, unless the parties mutually agree that a different form be used * * *."

Part 2 provides:

(a) "The arbitration of all disputes between Exhibitors and Distributors arising under any exhibition contract, if the parties shall agree on arbitration, shall be in accordance with the arbitration clause of the so-called Optional Standard License Agreement provided for in this Code, except as the provisions of such clause may be modified by the provisions of this Code."

We believe this development is persuasive that an arbitration clause is so essential a part of an exhibition contract that the business can not be conducted without one.

Point IV.

The Contracts Sued on Were Imposed by a Conspiracy of Motion Picture Distributors Controlling Upwards of 60 Per Cent of the Production and Distribution of Motion Pictures in the United States. Respondent Was Compelled to Buy Pictures on This Standard Form Containing a Vital Clause Which Is Admittedly Illegal as Well as Many Other Provisions Equally Oppressive.

1. *Respondent had no choice as to the form of contract.* Mr. Muller, lessee of the theatre in Maple Lake and the village furniture dealer, undertaker and plumber (R. 26, 41), testified that he was compelled to do business with parties to the conspiracy condemned in the *Paramount Case* and that he was unable to obtain pictures from any of those

companies on other than the Standard Form (R. 27-28, 39). The trial court made the following findings, among others, which were in effect sustained, or at least, not disturbed by the Supreme Court of Minnesota:

V.

"That prior to the making of said contract, as well as at the time of entering into same, said plaintiff, together with other producers and distributors of motion pictures, were members of said Motion Picture Producers and Distributors of America, and controlled 60% of the production and distribution of motion pictures in the United States produced and distributed for shipment and sale and commerce between the several states, and that all of said times, the said members of said Motion Picture Producers and Distributors of America, including plaintiff, together with other producers and distributors of motion pictures, being all members of the several Film Boards of Trade, organized and controlled by the said members of the Motion Picture Producers and Distributors of America, including this plaintiff, controlled at least 98% of the production and distribution of motion pictures in the United States, produced and distributed for shipment and sale and commerce between the several States.

VI.

That at all times herein mentioned, all exhibitors, including the defendant, engaged in exhibiting such motion pictures in theatres throughout the United States, were of necessity compelled to do business with said plaintiff, and said other producers and distributors controlling the production and distribution of said motion pictures in order to obtain motion pictures to carry on their business.

VII.

That in the year 1928, the plaintiff herein and said other producers and distributors of motion pictures so controlling 98% of the production and distribution of motion pictures for distribution and commerce between the several states, did agree with each other and with some exhibitors, including this defendant, through their duly authorized representatives, that they would distribute their product and motion pictures throughout the United States in a particular manner, to-wit, by means of the said standard exhibition contract and none other, and that no one would be permitted to sell, license or purchase or exhibit any motion pictures so produced and distributed within the United States, except under said plan and in conformity with the terms of said contract.

VIII.

That pursuant to said agreement among said producers and distributors, including plaintiff, it was then agreed by and among said producers and distributors, including plaintiff, that the terms upon which any of said distributors would sell, and any exhibitors, including defendant, would be permitted to purchase from said distributors, should be embodied in a form of contract known as the Standard Exhibition Contract; that none of the said distributors would sell or permit the exhibition of their product in the United States, except under the terms of said Standard Exhibition Contract, to be executed by the particular distributor and exhibitor in each instance; that the distributor and exhibitor were each required to warrant that the said predetermined terms were all contained in such con-

tract, and that no provision inconsistent with such predetermined terms was contained therein."

These findings, it is submitted, bring the entire contract within the condemnation of the Sherman Act. As stated by Judge Thacher in the *Paramount Case*, 34 Fed. (2d) 984, 989, "it is when agreements are sought to be imposed on others regardless of their wishes by coercive combinations having the power to say 'Take what is offered or get nothing' that they become illegal."

2. *The Standard Exhibition Contract contains many provisions in addition to Paragraph 18 which "unduly interfere with the free exercise of their rights by those engaged * * * in trade and commerce."* The words quoted in the caption are from the decision of this Court in *United States vs. Colgate & Co.*, 250 U. S. 300, 307, and were cited by Mr. Justice McReynolds in his opinion in the *Paramount Case*. They exactly describe many of the provisions in the contracts sued upon and which the Minnesota courts refused to enforce.

Without recounting the provisions paragraph by paragraph as was done under the preceding point, it is enough to point to a few of the more flagrant provisions of the contract:

A. Provision whereby the distributor is relieved of its obligation to deliver pictures contracted for by the expedient of (1) roadshowing such pictures or (2) delaying their general release (Par. Third-b).

B. Provision requiring exhibitors to pay in advance for all pictures (Par. Fourth).

C. Fixing the terms of "protection" (Par. Sixth).

D. Provision requiring exhibitor to feature the dis-

tributor's name in all newspaper and other advertising, to lease all advertising accessories from the distributor, and prohibiting subsequent run exhibitors to advertise pictures until the completion of their run in prior run theatres (Par. Twelfth).

E. Requiring exhibitors to pay all taxes based on the "delivery" as well as the "exhibition" of pictures (Par. Fourteenth).

F. Prescribing the admission prices to be charged by the exhibitors at their theatres (Par. Fifteenth; also Schedule, Pet. Br. App. A, p. 21).

G. Limiting valuable right to exclude pictures to exhibitors buying "an entire group of feature photoplays offered by the distributor to the exhibitor at one time, and not otherwise"—thus virtually compelling the exhibitor to buy the entire block of pictures offered by the distributor (Par. Twentieth).

These uniform provisions have been drafted by the distributors solely in their own interest. The manifest purpose was to crack the whip over the exhibitors, control the operating policy of the theatres and monopolize the playing time on the screens. Any variation as between distributors as regards these important provisions would have been a major competitive factor. No exhibitor in his right mind would have executed these contracts if more favorable contracts had been available. But there was no choice. It was "Take what is offered or get nothing."

We submit that, wholly aside from Paragraph 18, there is scarcely a provision in the Standard Exhibition Contract, imposed as it was by force, that does not reek with illegality or which a court could in good conscience enforce.

Point V.

The Contracts Sued on Are Unenforceable Because Wholly Lacking in Mutuality.

1. *Even if the supposed Federal question was erroneously decided, the judgment below should be affirmed for the reason that it can be sustained upon other grounds than those assigned by the Minnesota courts.*

Assuming but not conceding that the Supreme Court of Minnesota was mistaken in the reason assigned for its judgment in this case, it would be manifestly unfair to reverse that judgment if it can be sustained on other grounds not involving any conceivable Federal question. It is possible for courts to be correct in their judgments and wrong in their reasoning.

In *Walter A. Wood Co. vs. Skinner*, 139 U. S. 293, this Court speaking through Mr. Justice Brown said:

> "It is well settled by a long series of adjudications that, to give this Court jurisdiction by writ of error to a State court, it must appear affirmatively, not only that a Federal question was presented for decision to the highest court of the State having jurisdiction, but *that its decision was necessary to the determination of the case*, and that it was actually decided, or that the judgment rendered could not have been given without deciding it." *De Saussure vs. Gaillard*, 127 U. S. 216. (Italics ours.)

In *Waters-Pierce Oil Co. vs. Texas*, 212 U. S. 86, 106, Mr. Justice Day, speaking for the Court, said:

> "In thus deciding the Court of Civil Appeals did not determine a Federal question, nor necessarily decide one adversely to the plaintiff in error, controlling in

character, if it appears upon this record *that the verdict and judgment can stand upon other grounds,* free from objection, so far as Federal rights are concerned." (Italics ours.)

2. *The Standard Exhibition Contract is one of mutual promises; the promises of the exhibitor are made enforceable, the promises of the distributor are not, hence there is no mutuality.* In this case, the consideration moving from and to each party to the contract is the promise of the other party to the contract. In other words, respondent promises to accept certain pictures and to pay certain rentals therefor, in consideration of certain promises made by petitioner, all of which are contained in the contracts. Respondent makes a promise and his promise is consideration for petitioner's promise.

A promise is a good consideration for a promise, if it imposes upon the promissor some binding legal obligation. If if does not impose a legal obligation, then it is not a binding promise and hence not a good consideration.

13 *Corpus Juris,* p. 329, states the rule as follows:

> "A promise is a good consideration for a promise, provided always that it imposes some legal liability on the person making it. If it imposes none, then it can not be a consideration."

The contract in question (Second B) provides for the leasing of certain photoplays on condition that such photoplays having been produced, are generally released by it within a certain time therein designated. It also, under the heading "roadshows" reserves the right to roadshow any pictures produced and generally released, and to except the pictures not generally released or so roadshown from its obligation to furnish same to the respondent.

In other words, if the petitioner, as the producer and distributor of a photoplay, goes ahead and produces photoplays and discovers that the photoplays as produced are good money-making pictures, it has the right under the contract to roadshow such pictures, and by the terms of the contract, such pictures do not have to be furnished, and are excepted from the contract.

Again, if the picture should not be roadshown, but if for some reason petitioner decides not to generally release the picture during the life of the contract, it is not under any obligation to furnish the same to the respondent. It may delay the general release of a picture for a short time, put it in the next year's offering and sell it the following season at a higher rental. One party to this contract, the petitioner, has the power of determining whether it shall be bound; it has the power to say whether it will perform or will not perform; it has the right to live up to the contract, or to get out of the contract, as it sees fit.

Wherein is the petitioner unconditionally bound to perform? How can it be forced to furnish a picture if it decides to roadshow it or refuses to generally release it? Where is it under any obligation to perform, if it decides it is not to its interest to perform? Where is there mutuality of consideration? What then is the consideration for the respondent's promise? The fact of the matter is that there is none. It follows, therefore, that these contracts, lacking mutuality of consideration, are unenforceable.

The promise made by the petitioner is an illusory one.

It has been said by the Supreme Court of Minnesota in the case of *Bailey vs. Austrian*, 19 Minn. 535 (465):

> "If this set of facts establishes any contract, it is a contract of mutual promises; that is to say, the sole con-

sideration for defendant's promise to supply is plaintiff's promise to purchase, and vice versa.

The general rule (with exceptions not important in this instance) is "that a promise is not a good consideration for a promise, unless there is an absolute mutuality of engagement, so that each party has a right at once to hold the other to a positive agreement."

This must be taken as the law of Minnesota whose courts were invoked by the petitioner in this case.

The case at bar is a case of mutual promises. But the case at bar goes one step further, and the contracts contain the additional clause whereby one of the contracting parties can release itself from all obligations at its own convenience and upon its own election, while the other party has no such corresponding right. The courts have uniformly held that such contracts are void and of no effect.

The general rule is stated in 13 *Corpus Juris* 337-8, as follows:

"Where one person reserves the absolute right to cancel or terminate the contract at any time mutuality is absent, this rule being frequently applied to contracts of sale."

In the case of *Ellis vs. Dodge Bros.*, 237 Fed. 860, the court had for consideration an agreement which provided that it would expire by limitation on June 30, 1915, or may be cancelled by the manufacturer or dealer upon 15 days' written notice. The defense of lack of mutuality was raised in that case. The court held that the contract was void on two grounds, one of which was lack of mutuality with reference to the following provision in the contract: "This agreement shall expire by limitation June 30, 1915, or may be

cancelled by the manufacturer or dealer upon 15 days' written notice."

The court said:

> "This provision would be fatal to this agreement, as a binding contract between the parties, if it were not otherwise objectionable * * * To agree to do some thing and reserve the right to cancel the agreement at will is no agreement at all."

In *Nicholl vs. Wetmore,* 156 N. W. 319 (Ia.), the contract provided that the dealers might cancel the contract at any time, if in their judgment the sub-dealer was not properly promoting the sale of the cars, but no corresponding right was given to the sub-dealer. The court said:

> "The court speaks of the alleged contract as a 'jug-handled' affair, but which, even if it had been complete, there would be no mutuality of enforceable obligation. By section 3 of the instrument defendant reserved the absolute right to cancel the same if at any time, in their judgment, the defendant was not properly promoting the sale of their cars, but no corresponding right was reserved to the plaintiff * * * That contracts of this nature are clearly lacking in mutuality has been held in *Velie vs. Kopmeier,* 114 C. C. A. 284, 194 Fed. 324; *Oakland vs. Ind. Auto Co.,* 121 C. C. A. 319, 201 Fed. 499; *Goodyear vs. Koehler,* 159 App. Div. 116, 143 N. Y. Supp. 1046."

In the case at bar, the Fox Film Corporation also reserves the right to cancel the contracts whenever in their judgment it is desirable to do so by the simple expedient of not supplying the pictures.

The court, in the case of *Killebrew vs. Murray,* 151 S. W. 662 (Ky.), had for its consideration a contract involving a

mining lease. It was a phosphate mining lease for 10 years, which did not give the lessor the right to terminate the lease within that time, but permitted the lessee to begin work of prospecting and mining at any time within 10 years, and also contained the provision that the lessee might quit and cancel the contract or lease whenever he chooses to do so, upon notice to the lessor that the land does not contain paying qualities of phosphate in his opinion. The court, in its opinion, said:

> "Such contracts lack the mutuality essential to their validity. A unilateral executory contract is, in law, a *nudum pactum*, and is unenforceable. Where it is left to one of the parties to an agreement to choose whether he will proceed or abandon it, neither can specifically enforce it in equity."

In the *Great Northern Ry. Co. vs. Sheyenne Tel. Co.*, 145 N. W. 1062 (N. D.), it was held:

> "Contracts between a railroad company and a telephone company which give the latter the privilege of placing a telephone in two depots in consideration of free service for it, are not mutual where they are subject to termination at will of one with a stipulation that no corresponding right should be exercised by the other."

In this case the court also said:

> "In law actions mutuality is determined as of the time the contract is entered into."

In *American Agricultural Chemical Co. vs. Kennedy*, 48 S. E. 868 (Va.), the court said:

> "A contract by which plaintiff agrees to sell fertilizer, and defendants agree to buy, having no other consideration than their mutual promises, and providing that

plaintiff may cancel it at any time, is void for lack of mutuality of engagement, so that defendants may refuse to purchase, the plaintiff manufactures the fertilizer and puts it in sacks marked for them and makes tender thereof."

In discussing the rule of mutuality of obligation, with specific reference to contracts which involve a clause that one of the parties may cancel the contract, the court said in the case of *Combs vs. Hazard Ice and Storage Co.*, 290 S. W. 1034:

"No rule is more firmly settled than that mutuality of obligation is essential to the validity of an executory contract. Hence, where it is left to one of the parties to choose whether he will proceed or abandon the contract, and he may do so at any time, without incurring any liability thereunder, the contract is not binding upon either."

In *Powell vs. Ward*, 280 S. W. 151, the court said:

"Contract leasing half interest in coal mine, under which lessee was to pay royalty for coal sold of more than $3.00 a ton, he to have right to operate mine so long as he could make profit on coal, and right to turn it back to lessors on notice, held unilateral and unenforceable by him, except as already executed."

In the case of *Shortell vs. Evans-Ferguson Co.*, 277 Pac. 519 (Cal.), the court discusses the general rule which is stated in 13 *C. J.* 337, and which is quoted in the forepart of this memorandum, and on the question of the validity of such contracts, says:

"The general rule is stated in 13 *Corpus Juris* 337, supported by reference to a number of decisions, that

where one party reserves the right of cancellation, mutuality is absent * * * The right of appellant to withdraw from the agreement is clear. There was no mutuality of consideration provided for. On one hand, it was proposed to bind respondent in absolute terms to perform her part, while appellant's performance was made conditional * * * If a promise does not offer an enforceable legal right or forbearance it is not a consideration * * *."

In *City vs. Fidelity & Deposit Co.*, 267 Fed. 181, the court had for consideration a contract entered into by the city for the sale of certain bonds, which it contemplated selling on a certain day, but reserved to itself the right to terminate the contract, provided it did not dispose of the bonds. The court, in its opinion, stated as follows:

"The purpose of the city, as made apparent by the language of Section 11, was to reserve the right to terminate the contract, provided it did not dispose of the bonds, and in the exercise of such right, to escape any liability to any one upon any claim or demand whatever. A contract of such nature could not be enforced; it lacks mutuality."

Bankers Trust Co. vs. Farmers and Merchants Bank, 136 S. E. 143 (Ga.), was a case involving the construction of a contract entered into between the bank for the salary of its fiscal agent who could terminate the contract at any time, upon notice that he had become dissatisfied with the management or operation of the bank. He had rendered certain promotion services involved in this agreement. The court said:

"The contract described in third certified question is lacking in mutuality, because of the provision that the fiscal agent, one of the parties to the contract, may at

any time terminate the contract, should it 'become dissatisfied with the management and operation of said bank.'"

The provisions of the Standard Form discussed under Points III and IV further illustrate the one-sided nature of the document. We ask that the Court on this point consider not only the lack of mutuality in the undertakings of the parties, but all other features as well. Only through the combined action of the distributors controlling the pictures which exhibitors must have to operate their theatres could such a document be imposed on the exhibitors.

Point VI.

The Supreme Court of Minnesota Resolved No Federal Question But Merely Decided That an Admittedly Illegal Provision of the Standard Exhibition Contract Was Not Severable From the Remainder of the Contract.

The question submitted to and determined by the Supreme Court of Minnesota is thus defined in the opinion of that Court:

> "The question presented on this appeal is whether the arbitration clause is severable from the contract, leaving the remainder of the contract enforceable, or not severable, permeating and tainting the whole contract with illegality and making it void" (R. 79).

The illegality of Paragraph 18 is conceded. Petitioner has been most emphatic in asserting that this paragraph is no longer in the contract. "A practical deletion" is the phrase used in the application for reargument in the court below (R. 85). It is submitted that a determination of the rela-

tionship between this deleted paragraph and the remaining paragraphs involves no more than an interpretation of the contracts themselves and presents no Federal question.

This is evident from the labored effort to establish jurisdiction in Point IV of petitioner's brief (p. 23). Counsel is driven to the contention that the Supreme Court of Minnesota failed or refused to give full faith and credit to the decree in the *Paramount Case*. But that decree is not *res judicata* as we have already demonstrated (Point I, subhead 1); and the provisions relied upon do not have the effect for which petitioner contends as has also been demonstrated (Point I, subhead 2).

Obviously there can be no question of failure to give full faith and credit to a decree which is not binding on both parties. An examination of the decisions cited by petitioner in support of its contention makes this clear:

Knights of Pythias vs. Meyer, 265 U. S. 30;

St. Louis K. C. & C. R. Co. vs. Wabash R. Co., 217 U. S. 247.

The present case is clearly distinguishable from the above cases for the reason that the respondent, Muller, was not a party to the decree in the *Paramount Case* either by representation, succession or intervention.

The claim that the Supreme Court of Minnesota in deciding the question of severability (the only question submitted to it) failed or refused to follow the decisions of this Court in certain enumerated cases, even if true, does not raise a Federal question reviewable under Section 237 of the Judicial Code (U. S. Code, Sec. 344). But as shown under Point II, subhead 2 of this brief, the claim is without merit. The decision of the court below is wholly consistent with the decisions of this Court in the *Sewer Pipe, Wall Paper,*

Wilder and Small Cases, all of which were considered under Point II.

CONCLUSION.

It is respectfully submitted that the writ of certiorari herein should be dismissed for want of jurisdiction, or, in the alternative, that the judgment of Supreme Court of Minnesota should be affirmed.

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January 30, 1935.